

which must be acquired and maintained by a holding company affiliate to which a voting permit has been granted, see section 5144(b) and (c) of the Revised Statutes (12 U.S.C. 61).

NATURAL RESOURCES

DEDUCTIONS

§ 1.611-0 Regulatory authority.

Sections 1.611-1 through 1.614-8, inclusive, are prescribed under the authority granted the Secretary or his delegate by section 611(a) of the Code to prescribe regulations under which a reasonable allowance for depletion and depreciation of improvements shall be allowed, according to the peculiar conditions in each case, in the case of mines, oil and gas wells, other natural deposits and timber.

[T.D. 6965, 33 FR 10692, July 26, 1968]

§ 1.611-1 Allowance of deduction for depletion.

(a) *Depletion of mines, oil and gas wells, other natural deposits, and timber—*

(1) *In general.* Section 611 provides that there shall be allowed as a deduction in computing taxable income in the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion. In the case of standing timber, the depletion allowance shall be computed solely upon the adjusted basis of the property. In the case of other exhaustible natural resources the allowance for depletion shall be computed upon either the adjusted depletion basis of the property (see section 612, relating to cost depletion) or upon a percentage of gross income from the property (see section 613, relating to percentage depletion), whichever results in the greater allowance for depletion for any taxable year. In no case will depletion based upon discovery value be allowed.

(2) See § 1.611-5 for methods of depreciation relating to improvements connected with mineral or timber properties.

(3) See paragraph (d) of this section for definition of terms.

(b) *Economic interest.* (1) Annual depletion deductions are allowed only to the owner of an economic interest in mineral deposits or standing timber.

An economic interest is possessed in every case in which the taxpayer has acquired by investment any interest in mineral in place or standing timber and secures, by any form of legal relationship, income derived from the extraction of the mineral or severance of the timber, to which he must look for a return of his capital. For an exception in the case of certain mineral production payments, see section 636 and the regulations thereunder. A person who has no capital investment in the mineral deposit or standing timber does not possess an economic interest merely because through a contractual relation he possesses a mere economic or pecuniary advantage derived from production. For example, an agreement between the owner of an economic interest and another entitling the latter to purchase or process the product upon production or entitling the latter to compensation for extraction or cutting does not convey a depletable economic interest. Further, depletion deductions with respect to an economic interest of a corporation are allowed to the corporation and not to its shareholders.

(2) No depletion deduction shall be allowed the owner with respect to any timber, coal, or domestic iron ore that such owner has disposed of under any form of contract by virtue of which he retains an economic interest in such timber, coal, or iron ore, if such disposal is considered a sale of timber, coal, or domestic iron ore under section 631 (b) or (c).

(c) *Special rules—*(1) *In general.* For the purpose of the equitable apportionment of depletion among the several owners of economic interests in a mineral deposit or standing timber, if the value of any mineral or timber must be ascertained as of any specific date for the determination of the basis for depletion, the values of such several interests therein may be determined separately, but, when determined as of the same date, shall together never exceed the value at that date of the mineral or timber as a whole.

(2) *Leases.* In the case of a lease, the deduction for depletion under section 611 shall be equitably apportioned between the lessor and lessee. In the case of a lease or other contract providing